

January 7, 1938

Dear Jerry:

Your letter of December 28 and its enclosures raise several questions to which the Commission has devoted considerable attention. I assume that you desire my comments primarily upon Mr. Ryan's suggestion that Congress "liberalize the sale of securities", and therefore I have confined myself to that aspect of his letter.

If Mr. Ryan means to suggest a relaxation of the requirements of the Securities Act of 1933 that all important information relating to public offerings of securities be disclosed to prospective investors, I can only reply that it seems to me to be the primary purpose of that Act to prevent the sale of securities which cannot be disposed of in the light of a full and fair disclosure of the characteristics of the securities and their issuer. The Commission constantly has sought to simplify its forms for registration, and to require the disclosure of only such information as appears to be essential for a fair evaluation of the securities being offered. It is true that the so-called "twenty day waiting period" between the filing of a registration statement and its effective date may delay the date of an offering to some extent, but I do not believe it can be seriously contended that a delay of one month or possibly two in the sale of securities is an excessive price to pay for the protection of the investing public which flows from the operation of the Securities Act of 1933.

Perhaps Mr. Ryan is under the impression that the Securities Act has greatly increased the expenses involved in the sale of an issue of securities. From time to time the Commission has published the results of statistical studies made by its Research Division, some of which cast light upon the question of the cost of registering and selling securities. I am enclosing herewith Statistical Series Releases No. 30 and No. 41, together with the material referred to in the latter. Table III of Release No. 30 shows in detail the expenses of registration and flotation (other than underwriting commission and discount) of stock and bond issues of \$1,000,000 or more. You will note that the expenses properly attributable to compliance with the requirements of the Securities Act are negligible in amount. Similar data is contained in Item 4 of the leaflets referred to in Release No. 41. This table contains information relating to expenses of flotation of small as well as large issues. Here again you will observe that expenses other than commission and discount are comparatively small, and that only a very small percentage of that small amount is chargeable to the registration and prospectus requirements of the Securities Act.

As you are aware, Section 3(b) of the Securities Act conferred upon the Commission a limited discretionary power to establish exemption for securities

where the aggregate amount of the offering does not exceed \$100,000. For your convenience in replying to Mr. Ryan, I am enclosing two copies of the Securities Act. Section 3(b) appears on page 5 thereof.

The scope and purpose of Section 3(b) was described as follows in H.R. Rep. No. 85, 73d Cong. 1st Sess.:

“Subsection (b) gives a general authority to the Commission to ass to the class of express exemptions any security which because of the small amount involved or the limited character of the public offering should properly be excluded from the provisions of the act. To confer such a power upon the Commission permits the Commission by adequate rules and regulations to provide against needless registration of issues of such an insignificant character as not to call for regulation. This general power of the Commission, however, it closely limited by the requirement that it shall not extend to any issue whose aggregate amount exceeds \$100,000. The Commission is thus safe-guarded against any untoward pressure to exempt issues whose distribution may carry all the unfortunate consequences that the act is designed to prevent.” (p. 15)

Elsewhere in the Report the Commission was warned that

“This power is deemed necessary for the effective administration of the bill, but is expected to be used only in a sparing manner, which keeps in mind the prima facie requirement that every security and transaction not specifically exempted by the terms of the bill should be kept within its scope.” (pp. 6-7)

In accordance with this principle, the Commission has adopted a number of rules exempting limited amounts of certain classes of securities on specified conditions. These rules appear in Regulation A of the enclosed General Rules and Regulations under the Securities Act, beginning at page 7. In promulgating rules pursuant to Section 3(b), the Commission has sought to give effect to the opinion of Congress that in certain circumstances it is desirable to relieve small offerings of securities from some or all of the burdens incident to registration, which burdens bear relatively more heavily upon small than large issues.

For your information, I shall describe briefly the terms and scope of the exemptions most frequently availed of for small offerings to be sold for cash. As you will note, Rule 200 in general exempts securities of new corporations which propose to operate with a capital of less than \$30,000, and securities of established corporations which desire to expand to an extent not requiring more than \$50,000 of securities to be sold.

Offerings which meet the terms and conditions of Rule 201 are relieved from practically all the requirements generally imposed by the Securities Act, including

the use of a prospectus containing specified information. To some degree, this privilege is in derogation of the purpose of the Securities Act with respect to dissemination of relevant information regarding public offerings of securities; consequently, its exercise has been confined to situations in which reason and experience seem to indicate relatively little danger of abuse.

On the other hand, Rule 202 is designed to exempt securities which -- although they may be fully as meritorious as those eligible for exemption under Rule 201 -- do not possess all of the characteristics which are regarded as essential to justify the unusual privileges conferred by exemption under Rule 201. Nevertheless, you will note that even the requirements for exemption under Rule 202 are not difficult to comply with, and impose upon the issuer only a slight burden of expense and trouble. You will be interested to know during the fiscal year ended June 30, 1937, 475 issues, involving offerings totaling \$37,734,416, were exempted under Rule 202 and other less used rules. In addition, an undeterminable amount of securities were offered and sold without registration under the Securities Act by virtue of exemption under Rule 200, Rule 210, or one of the other rules not requiring any prospectus or other material to be filed with the Commission.

I trust that these will aid you in replying to Mr. Ryan's letter, which I am returning herewith. If I can be of further service at any time, please do not hesitate to call upon me.

Yours faithfully,

William O. Douglas
Chairman

The Honorable Jerry Voorhis
139 Old House Office Building
Washington, D.C.

Enclosures:

Stat. Series Rel. Nos. 30 and 41 (and tables referred to in the latter)

3 Copies of SA

3 Copies of Gen. Rules and Regs. SA

Mr. Ryan's letter